

§ 75.436

(1) The costs are reasonable and necessary in relation to the administration of the Federal award and activities required to deal with the proceeding and the underlying cause of action;

(2) Payment of the reasonable, necessary, allocable and otherwise allowable costs incurred is not prohibited by any other provision(s) of the Federal award;

(3) The costs are not recovered from the Federal Government or a third party, either directly as a result of the proceeding or otherwise; and,

(4) An authorized Federal official must determine the percentage of costs allowed considering the complexity of litigation, generally accepted principles governing the award of legal fees in civil actions involving the United States, and such other factors as may be appropriate. Such percentage must not exceed 80 percent. However, if an agreement reached under paragraph (c) of this section has explicitly considered this 80 percent limitation and permitted a higher percentage, then the full amount of costs resulting from that agreement are allowable.

(f) Costs incurred by the non-Federal entity in connection with the defense of suits brought by its employees or ex-employees under section 2 of the Major Fraud Act of 1988 (18 U.S.C. 1031), including the cost of all relief necessary to make such employee whole, where the non-Federal entity was found liable or settled, are unallowable.

(g) Costs of prosecution of claims against the Federal Government, including appeals of final HHS agency decisions, are unallowable.

(h) Costs of legal, accounting, and consultant services, and related costs, incurred in connection with patent infringement litigation, are unallowable unless otherwise provided for in the Federal award.

(i) Costs which may be unallowable under this section, including directly associated costs, must be segregated and accounted for separately. During the pendency of any proceeding covered by paragraphs (b) and (f) of this section, the Federal Government must generally withhold payment of such costs. However, if in its best interests, the Federal Government may provide

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for conditional payment upon provision of adequate security, or other adequate assurance, and agreement to repay all unallowable costs, plus interest, if the costs are subsequently determined to be unallowable.

§ 75.436 Depreciation.

(a) Depreciation is the method for allocating the cost of fixed assets to periods benefitting from asset use. The non-Federal entity may be compensated for the use of its buildings, capital improvements, equipment, and software projects capitalized in accordance with GAAP, provided that they are used, needed in the non-Federal entity's activities, and properly allocated to Federal awards. Such compensation must be made by computing depreciation.

(b) The allocation for depreciation must be made in accordance with appendices III through IX.

(c) Depreciation is computed applying the following rules. The computation of depreciation must be based on the acquisition cost of the assets involved. For an asset donated to the non-Federal entity by a third party, its fair market value at the time of the donation must be considered as the acquisition cost. Such assets may be depreciated or claimed as matching but not both. For the purpose of computing depreciation, the acquisition cost will exclude:

(1) The cost of land;

(2) Any portion of the cost of buildings and equipment borne by or donated by the Federal Government, irrespective of where title was originally vested or where it is presently located;

(3) Any portion of the cost of buildings and equipment contributed by or for the non-Federal entity, where law or agreement prohibits recovery; and

(4) Any asset acquired solely for the performance of a non-Federal award.

(d) When computing depreciation charges, the following must be observed:

(1) The period of useful service or useful life established in each case for usable capital assets must take into consideration such factors as type of construction, nature of the equipment, technological developments in the particular area, historical data, and the

renewal and replacement policies followed for the individual items or classes of assets involved.

(2) The depreciation method used to charge the cost of an asset (or group of assets) to accounting periods must reflect the pattern of consumption of the asset during its useful life. In the absence of clear evidence indicating that the expected consumption of the asset will be significantly greater in the early portions than in the later portions of its useful life, the straight-line method must be presumed to be the appropriate method. Depreciation methods once used may not be changed unless approved in advance by the cognizant agency. The depreciation methods used to calculate the depreciation amounts for indirect (F&A) rate purposes must be the same methods used by the non-Federal entity for its financial statements.

(3) The entire building, including the shell and all components, may be treated as a single asset and depreciated over a single useful life. A building may also be divided into multiple components. Each component item may then be depreciated over its estimated useful life. The building components must be grouped into three general components of a building: building shell (including construction and design costs), building services systems (*e.g.*, elevators, HVAC, plumbing system and heating and air-conditioning system) and fixed equipment (*e.g.*, sterilizers, casework, fume hoods, cold rooms and glassware/washers). In exceptional cases, a cognizant agency may authorize a non-Federal entity to use more than these three groupings. When a non-Federal entity elects to depreciate its buildings by its components, the same depreciation methods must be used for indirect (F&A) purposes and financial statements purposes, as described in paragraphs (d)(1) and (2) of this section.

(4) No depreciation may be allowed on any assets that have outlived their depreciable lives.

(5) Where the depreciation method is introduced to replace the use allowance method, depreciation must be computed as if the asset had been depreciated over its entire life (*i.e.*, from the date the asset was acquired and

ready for use to the date of disposal or withdrawal from service). The total amount of use allowance and depreciation for an asset (including imputed depreciation applicable to periods prior to the conversion from the use allowance method as well as depreciation after the conversion) may not exceed the total acquisition cost of the asset.

(e) Charges for depreciation must be supported by adequate property records, and physical inventories must be taken at least once every two years to ensure that the assets exist and are usable, used, and needed. Statistical sampling techniques may be used in taking these inventories. In addition, adequate depreciation records showing the amount of depreciation taken each period must also be maintained.

§ 75.437 Employee health and welfare costs.

(a) Costs incurred in accordance with the non-Federal entity's documented policies for the improvement of working conditions, employer-employee relations, employee health, and employee performance are allowable.

(b) Such costs will be equitably apportioned to all activities of the non-Federal entity. Income generated from any of these activities will be credited to the cost thereof unless such income has been irrevocably sent to employee welfare organizations.

(c) Losses resulting from operating food services are allowable only if the non-Federal entity's objective is to operate such services on a break-even basis. Losses sustained because of operating objectives other than the above are allowable only:

(1) Where the non-Federal entity can demonstrate unusual circumstances; and

(2) With the approval of the cognizant agency for indirect costs.

§ 75.438 Entertainment costs.

Costs of entertainment, including amusement, diversion, and social activities and any associated costs are unallowable, except where specific costs that might otherwise be considered entertainment have a programmatic purpose and are authorized either in the approved budget for the